Perpetual Private | Quarterly Market Update

"Shock and yawn"

Is the market putting all its chips on a few squares?

September 2025

Trust is earned.

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Executive summary

2025 has been a challenging year. With the new Trump administration proving to be far more bombastic than had been widely expected, combined with elevated geopolitical tensions, persistent inflation, trade uncertainty and a once-in-a-lifetime technological advance; investment markets have been exceedingly resilient. Indeed, in the face of these shocks, to name but a few, we are seeing shares reach all-time highs, as well as other asset classes also delivering buoyant returns – outcomes you would normally expect in more idyllic conditions.

The three-month period to the end of September was one in which investors appeared to embrace the uncertainty, with an apparent devil-may-care attitude to the persistent deluge of challenges to historic norms. The emergence of Artificial Intelligence (AI) has undoubtably helped fuel the optimism, but so too has the resilience of labour markets and consumer spending.

Over the quarter and indeed the rolling 12-month period, all of the major asset classes we allocate to have enjoyed positive returns. This supports our sense that whilst we are somewhat uncomfortable in-the-market, being out-of-the-market would be equally uncomfortable.

As investors, we find this environment to be as compelling as it is concerning. Whilst our prudence compels our caution, we also recognise conditions as being consistent with meaningful short-term returns.

As we face into the final months of 2025, particularly with the likelihood of the traditional 'Santa Claus' rally, we expect our diligence and the discipline in our research efforts will serve us well. Whilst we certainly seek to enjoy as much as we can of any investment upside, we recognise that avoiding any correction, as much as that is possible, will be equally important.

In the following pages, we discuss what we see as some of the more important aspects of Artificial Intelligence, before diving into the state of the global economy and the near-term investment outlook, finishing with a focus on each of our primary asset classes.

Asset class snapshot

Australian equities

Australian shares advanced steadily through the September quarter, with the S&P/ASX 300 rising 5.0%[1] and delivering a 10.8% return over the past 12 months. Smaller companies outperformed, as the ASX Small Ordinaries surged 15.3%[2] for the quarter and over 21% year-on-year, driven by robust flows into emerging resource stocks and support from lower interest rates. Inflation, GDP growth and an increase in the rate of household spending has created an environment that is tempering the possibility of near-term easing by the Reserve Bank of Australia (RBA. Sector performance was mixed: Materials (+21.2%[3]) led, fuelled by gold miners and base metals, while Consumer Discretionary (+9.6%[4]) and Utilities (+11.4%[5]) also performed well. Energy (-1.0%[6]), Health Care (-9.7%[7]) and Consumer Staples (-1.4%[8]) lagged. Financials ex-Real Estate Investment Trusts (REIT) gained 1.3%[9], and Technology returned 2.2%[10]. Value stocks outperformed Growth (+8.8%[11] vs –3.9%[12]), reflecting strength in commodity and resource-linked names.

International equities

International shares climbed 6.4%[13] for the quarter and 2.3% in the month of September, defying seasonal weakness amid a complicated economic and geopolitical landscape. Markets have shifted focus from trade tensions, particularly Trump's earlier tariff threats, to the transformative potential of AI. This optimism has driven Growth stocks to outperform Value, with quarterly returns of 7.4%[14] vs 4.7%[15] and annual returns of 28.1% vs 17.2%. Leading sectors include Information Technology and Communication Services, returning 11.5%[16] and 10.5%[17] respectively. Consumer Discretionary also performed well at 8.4%[18], while smaller companies outpaced larger peers. However, Consumer Staples declined by 2.9%[19], and Real Estate and Health Care posted only modest gains as inflation and interest rate pressures persisted. Regionally, Hong Kong's Hang Seng index led with a 12.4%[20] return, surpassing the Nasdaq's 11.4%[21], supported by Chinese government buying through state-owned enterprises and tech sector momentum. Germany's DAX lagged slightly, returning -0.1%[22] for the quarter despite strong annual performance.

Real estate

Listed Real Estate delivered solid but uneven gains over the September quarter. Australian REITs (A-REITs) rose 4.8%[23], recapturing year-to-date positives before softening in late September as "higher-for-longer" inflation dampened valuations. Globally, REITs (G-REITs) gained 3.0%[24] for the quarter and 4.5% year-to-date, with notable regional contrasts: Japan surged 9.9%[25], while Germany fell nearly 10%[26]. At the sector level, office assets are stabilising from their trough while industrials are easing from peak conditions. Retail remains resilient, supported by firm consumer demand, whereas residential continues to underperform despite structural housing shortages across major economies. Healthcare rebounded albeit modestly.

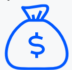
Refer to footnotes' description on page 29

Growth alternatives

The September quarter saw renewed signs of activity across private markets. Exit momentum improved after a quiet first half, though fundraising remained challenging for many managers. Deal values were supported by large transactions such as the US$55 billion take-private of Electronic Arts. Continuation vehicles continued to gain traction as managers seek to return capital to investors, and are increasingly viewed as co-investment-style structures that align interests between general and limited partners. Regionally, Europe remains attractive relative to North America, with more compelling entry valuations and European fiscal stimulus potentially underpinning demand. Real estate conditions remain uneven but are showing stability with cap-rate expansion likely having peaked. Infrastructure also saw an uptick in demand following earlier softness, while traded markets continued to exhibit pricing dispersion, supporting opportunities in relative-value hedge fund strategies.

Defensive alternatives

Private credit markets remained buoyant through the quarter, with strong demand continuing to compress spreads. Fixed-rate exposures benefited from lower policy rates, while broadly syndicated loans generated healthy margins above cash. Deal activity was subdued but steady, supported by ongoing refinancing and recapitalisation needs. Defaults remain low, although out-of-court restructurings have become more frequent, reflecting a proactive approach to managing corporate stress. In the insurance-linked space, activity picked up modestly, while catastrophe bond spreads remain attractive relative to traditional income assets. Specialty finance continued to perform well and remains a key area of opportunity under active review. Meanwhile, the regulatory capital segment, which allows banks to transfer credit risk on select loan portfolios to external investors, remains complex but offers appealing yield premia for the risks involved.



Fixed income

Fixed income markets recorded modest gains over the three month period as central banks continued to cut rates amid lingering inflation and resilient growth. Global bonds rose 1.0%[27], while Australian fixed income gained 0.4%[28], supported by easier policy but capped by higher-than-expected inflation and stronger domestic growth. The RBA's third cut of the year, to 3.60%, was followed by a rise in yields as inflation remained sticky, flattening the curve and limiting sovereign returns. In the US, the Federal Reserve cut rates twice as labour market data softened, prompting short-end yields to fall while longer maturities stayed anchored by fiscal and inflation concerns. Across Europe, 10-year yields in Germany and France rose on debt-sustainability worries. Credit outperformed sovereigns, with Australian credit returning 0.9%[29], global Investment Grade credit up 2.0%[30], and High Yield gaining 2.5%[31], supported by healthy corporate balance sheets, low defaults, and strong demand for carry, though spreads remain near historical tights, leaving little margin for disappointment if growth slows.

Refer to footnotes' description on page 29

Australian cash rate

The RBA lowered the cash rate by 25 basis points to 3.60% at its August meeting, marking the third quarterly cut since the easing cycle began in February. The move was consistent with earlier guidance that the RBA would lower rates gradually, balancing inflation control with support for growth. Inflation has broadly moderated but surprised to the upside in August, with headline CPI at 3.0% Year on Year (YoY)[32]. This sits just within the RBA's target range and is indicative of lingering price pressures. Labour market data softened modestly, with participation and total employment edging lower, though the unemployment rate held steady at 4.2%, still low by historical standards. The RBA noted that the labour market remains "a little tight" and reiterated its cautious, data-driven approach, signalling a willingness to adjust the pace of easing if inflation or global conditions diverge materially from expectations.

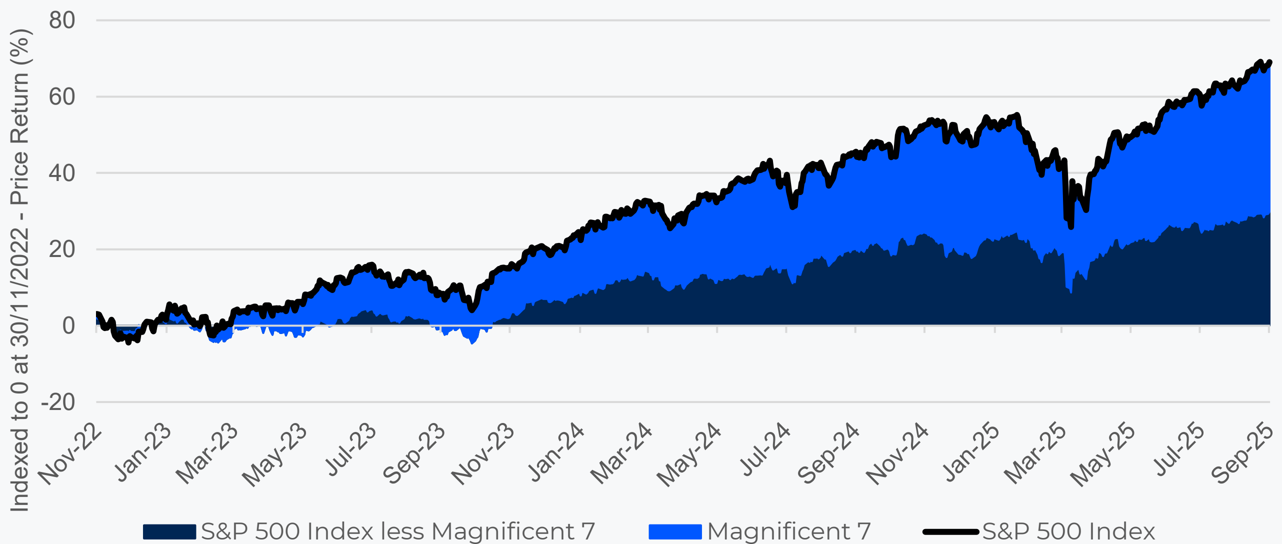
Australian dollar

The Australian dollar (AUD) appreciated 1.1% against the US dollar (USD) over the September quarter, closing near US$0.66. Volatility persisted, though less pronounced than in the first half of the year, with the AUD/USD trading between US$0.64 and US$0.67. The currency pair weakened through July and August as strong US growth data and robust corporate earnings supported the USD, before recovering into quarter-end. Domestically, the RBA's rate cut in August initially pressured the currency, though a stronger-than-expected CPI print (+3.0% YoY) dampened expectations for further easing. Meanwhile, concerns about a softening US labour market prompted the US Federal Reserve to cut rates twice during the quarter, putting mild downward pressure on the USD. The US Dollar Index, a measure of the greenback's value against a basket of major currencies, was broadly flat, marking a pause after a material weakening earlier in the year.

Special article - The AI paradox: When growth feeds on itself

Markets have a tendency to fall in love with singular narratives. In the late 1990s, it was the internet. Before that, it was the Japanese industrial dominance in the '80s, and go back far enough, it was the Nifty Fifty in the '60s. Today, it is artificial intelligence.

Nowhere is this clearer than in the performance of the so-called "Magnificent Seven" stocks (Apple, Microsoft, Alphabet, Amazon, Meta, Nvidia, and Tesla). Since the launch of ChatGPT on 30 November 2022, these seven companies have accounted for over half of the S&P 500's growth and now represent nearly a third of its total market capitalisation.



Source: S&P Global, Macrobond, Perpetual Private

For investors, the question isn't whether AI will be transformational. It clearly will be. The question is whether the extraordinary sums being deployed will generate genuine returns, or whether we're watching a capital-fuelled arms race where conviction runs well ahead of profitability.

The closed loop problem

Today's AI economy is starting to look less like an open market and more like a closed ecosystem. The same handful of companies are building the chips, training the models, operating the cloud infrastructure, and funding the start-ups that use it all.

Nvidia sells GPUs to Microsoft, Amazon, and Google. Those companies run the chips in their data centres to power AI start-ups like OpenAI. OpenAI then licenses its models back to Microsoft. Meanwhile, Nvidia buys cloud services from CoreWeave – a company it partly owns. Oracle, AMD, and even the US government are woven into these relationships through financing arrangements, subsidies, or joint ventures.

Here are just a few of the interconnected deals announced between the AI-linked companies in 2025...and the numbers are staggering.

Relationship	Announcement Date	Description
Nvidia and OpenAI	September 2025	Nvidia agrees to invest up to US$100 billion in OpenAI.
OpenAI and Oracle	September 2025	OpenAI inks a US$300 billion cloud deal with Oracle.
Nvidia and CoreWeave	September 2025	Nvidia buys US$6.3 billion of cloud services from CoreWeave for cloud computing service.
OpenAI and CoreWeave	March 2025	OpenAI to pay CoreWeave as much as US$22.4 billion.
OpenAI and AMD	October 2025	OpenAI agrees to deploy billions of dollars' worth of AMD chips.
US and Intel	August 2025	US takes a 10% stake in Intel using CHIPS Act funding.
Nvidia and Intel	September 2025	Nvidia invests US$5 billion in Intel and plans to co-develop chips.
US and Nvidia	August 2025	US takes a 15% cut of Nvidia and AMD's chip sales to China.

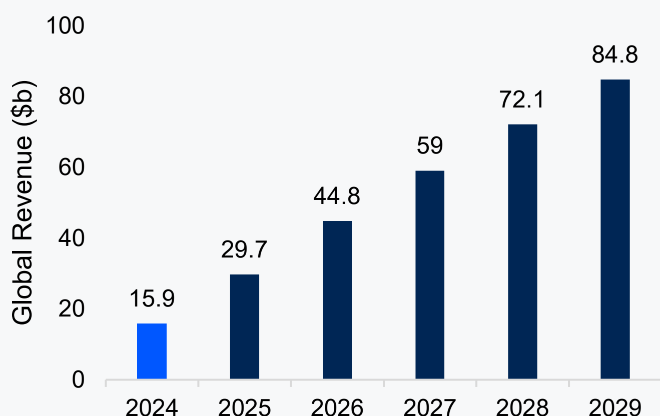
These aren't arm's-length transactions between independent buyers and sellers. They are a tightly woven web where the same dollar often appears across multiple revenue lines, investment portfolios, and valuations. Some call it a virtuous cycle. Others see a feedback loop where rising valuations justify more spending, which justifies higher valuations.

This pattern isn't unprecedented. During the late 1990s, telecom equipment vendors like Lucent and Nortel lent billions to customers who couldn't afford their gear. The loans appeared as revenue, demand looked robust, and share prices soared. For a while, the illusion held, until it didn't. Now, AI start-ups are leasing tens of billions in computing power from the same hyperscalers that fund them. The structure may be different, but the circular logic is somewhat familiar. Should investors consider this real demand, or manufactured momentum?

The capital expenditure arms race

The scale of AI-related spending is breathtaking. Bank of America projects global AI capex will hit US$414 billion in 2025, and Morgan Stanley projects nearly US$3 trillion will be spent globally on AI infrastructure by 2028. In contrast, revenue from generative AI is expected to be US$72 billion by that time. That's not profit, just top-line sales.

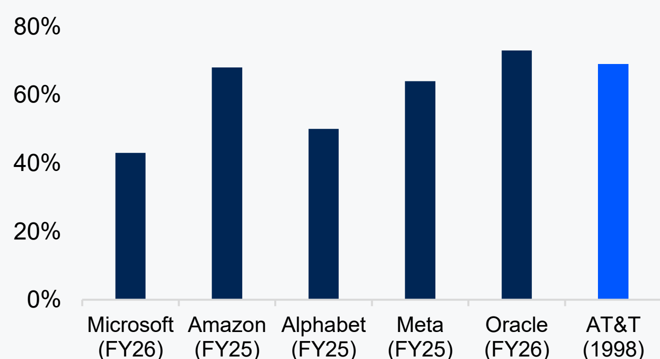
Chart 1: Forecast global revenue from generative AI



Source: As of April 2025. S&P Global, Perpetual Private.

The logic driving this buildout is defensive. According to their respective CEOs, no major technology company can afford to be caught without sufficient AI capacity if or when demand finally materialises. But the spending is already consuming over 65% of EBITDA for some of the largest players – higher than telecoms (i.e. AT&T) at the peak of the 1990s boom, while generating a fraction of that in incremental revenue.

Chart 2: CapEx (% of EBITDA)



Source: GQG Partners LLC, Bloomberg. Data from 1997 to 2025.

None of this would be alarming if cash flows were accelerating in parallel. But most AI applications remain unprofitable. This creates a troubling dynamic whereby spending is justified by anticipated future demand, but much of today's "demand" is internally generated.

Everyone is building now to avoid missing out later. That's a reasonable strategy, until everyone is doing it simultaneously. Then it becomes an arms race with no clear finish line and very uncertain economic returns.

The mathematics are sobering. One recent analysis projects that global AI and AI related capital expenditures may reach US $5.2 trillion by 2030. To justify that kind of outlay, companies will need not just massive revenue growth, but substantial profits, enough to recoup upfront investments after accounting for ongoing costs. Getting there requires either a dramatic acceleration in paying customers, sharply higher payments per user or a sharp contraction in expectations.

Lessons from the last boom

Today's situation isn't a replay of 2000. The current tech giants have genuine cash flows, diversified revenue streams, and defensible competitive advantages. Their balance sheets are strong. They're not burning through venture capital with no path to profitability.

However, the underlying pattern of overbuild-then-rationalise is eerily similar. Back then, companies laid enough fibre-optic cable to circle the globe hundreds of times over. Most of it went unused for years. Eventually, that excess capacity enabled cloud computing, video streaming, and the modern internet. The infrastructure wasn't wasted but it was wildly premature.

We may be seeing the same dynamic now. Today's data centres and GPU clusters could form the backbone of an AI-powered economy a decade from now. But the buildout does appear to be running far ahead of monetisation. And for investors, timing is everything.

There's another parallel worth noting. A recent survey found that over 75 per cent of AI researchers doubt that current approaches will lead to Artificial General Intelligence, the transformative breakthrough markets seem to be pricing in. This matters because investor expectations are built on assumptions about AI's trajectory that many experts consider optimistic at best.

The gap between what markets are pricing and what specialists believe is achievable should give investors pause. Breakthroughs may come but they rarely arrive on the schedule capital markets demand.

What this means for investors

So how should investors think about AI exposure in their portfolios?

The reality is that few portfolio managers can afford to be underweight AI linked investments in aggregate while they're driving the majority of index returns. Staying long in a momentum-driven market is rarely a career-limiting move. But being short at the wrong time can be fatal. In 2023, roughly 80% of professional economists predicted a recession that never materialised. Those that heeded their advice and positioned defensively paid a steep price in underperformance. So capital keeps flowing in, not always out of conviction, but because the alternative feels riskier.

This is how bubbles sustain themselves longer than fundamentals suggest they should. They don't burst when valuations become stretched. They deflate when leverage dries up, capital flows reverse, or a shock forces a reassessment.

When corrections do come in highly concentrated markets, they tend to be swift and indiscriminate. Correlations spike toward one, assets that should have low correlation move in lockstep with one another. In such scenarios, the exit is always narrower than the entrance.

Could AI deflate gently? Perhaps. Maybe the Magnificent Seven and other AI linked investments plateau, capital rotates into second-tier beneficiaries, and new public offerings like OpenAI provide fresh entry points. But more often than not, markets don't manage soft landings when valuations are stretched and positioning is crowded.

Still, we may be closer to 1995 than 1999. In the mid-'90s, critics were already warning of irrational exuberance, yet the market went on to rally for another five years. That's the danger with trying to time corrections. Bubbles can stay inflated far longer than reason allows, and far more money has been lost waiting for downturns than in the downturns themselves.

None of this means investors should abandon AI exposure entirely. The technology will reshape industries, workflows, and productivity over the coming decade. But the current financial structure supporting it looks increasingly fragile. Valuations are being justified by capital expenditure, which in turn is being justified by those same valuations, a loop of confidence that feels more circular than sustainable.

Investors would do well to remember that in every cycle, the challenge isn't knowing whether it will continue, it's making sure you're positioned for what comes after.

Shock and yawn

"Better than feared, but worse than we need."
Kristalina Georgieva, Managing Director, International Monetary Fund (IMF)

Duality

2025 will likely have an important place in the history books. As we face into the final months of the year, it is fair to say that this has been a time of disruption. Whether we focus on the norm-breaking behaviour of the US president, or pan the world more widely, it is clear that we have left the post WWII equilibrium and are searching for a new point of balance.

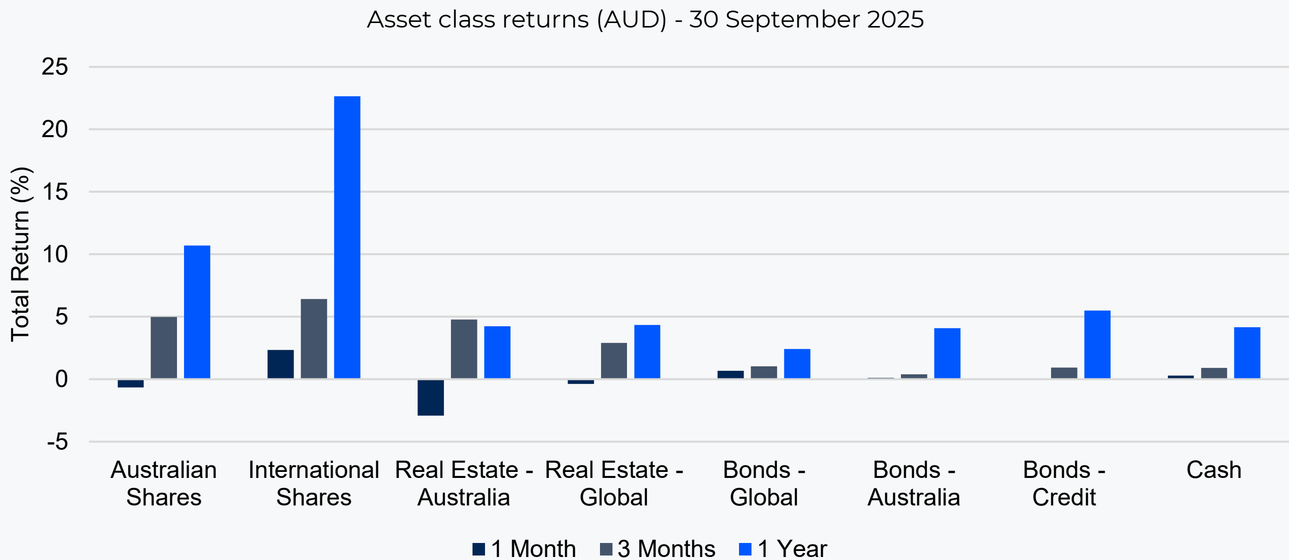
Certainly, Artificial Intelligence is a large and obvious part of what is going on (see our Special Article), but it takes only a moment's contemplation to recognise that this isn't the only factor at play. Whether we view the world from a political, geopolitical or economic point-of-view, we can find traces of what is happening today, well before the 2020 COVID pandemic. Perhaps in a few decades time it will be determined that Donald Trump's 2015 election victory was the signal (and potentially the catalyst), of a change away from the practices and structures that had rebuilt the world in the aftermath of two world wars. Whether he is part of the cause, or merely a symptom remains to be seen, but his combative and mercantilist nature has certainly changed what was a broadly cooperative landscape, into a competitive one.

Root causes however, are a discussion for another day. Our focus is on the nearer term; of the 2025 September quarter, and the balancing act that investors must face as we head into the end of the year and begin to peer into 2026. We believe that our opening quote from IMF Managing Director, Kristalina Georgieva, captures the moment well, when in her opening speech to launch the fund's latest World Economic Outlook at its annual meeting alongside the World Bank, she described global growth as "better than feared, but worse than we need".

Kristalina's description of global growth reflects a feature of the present moment, that we have been discussing in our investment meetings for months, and that is a sense of duality. Simply, the investment environment isn't either good or bad, but both good AND bad.

Reflecting on the quarter, if one had been isolated from today's 24-hour news cycle, they would be forgiven for thinking that it had been a period of idyllic economic and investment conditions. Here in Australia, shares were up 5.0%[1] for the three-month period, and 10.8% over 12 months. Internationally, the picture was very much the same. Globally (as reflected by the MSCI All Country World index) stock markets were up 6.4%[13] over the quarter and 22.8% over the year. Drilling into individual regions, the US continues to ride the AI boom with the broad S&P 500 index returning 6.8% over three months, whilst the tech-heavy Nasdaq gained 10.2%[21]. In Europe, Germany saw a mild consolidation, falling 1.1%[22] in the quarter, after a strong year (36.2%), and France which is facing into yet another political 'crisis' limped through with a tepid 2.1%, despite which the region as a whole still managed to deliver 4.6%. Hong Kong's Hang Seng index, which for the past couple of years has faced the dual challenges of a collapsing Chinese property market (some reports suggest as many as 90m apartments might be vacant) and being at the nexus of US/China trade tensions, saw an impressive 12.2%[20] over three months and is the best performing developed market that we monitors with a return of 37.2% over twelve months. We could continue but suffice to say, these buoyant outcomes are not confined only to shares of large companies. When we look at smaller company indices or even across asset classes, returns are impressively robust for the majority of asset groupings and segments.

Chart 3: Asset class returns



Source: FactSet, Returns are in AUD. As of 30 June 2025. All returns are in AUD. Past performance is not indicative of future performance. Indices: Real Estate – Australia: ASX 300 / A-REIT, Real Estate – Global: FTSE EPRA Nareit Global, Bonds – Global: Bloomberg Global Aggregate, Bonds - Global Credit: Bloomberg Global High Yield, Bonds – Australia: Bloomberg AusBond Composite (0+Y), Bonds - Australian Credit: Bloomberg AusBond Credit (0+Y), Cash: Bloomberg AusBond Bank Bill

Shock and yawn

Before considering what might be driving the carefree demeanour of markets, it is worth considering the multitude of complications investor sentiment currently carries. Matters that in prior decades would have been inherently shocking are achieving a few days half-life in today's news cycle, before being quickly forgotten (or 'yawned' off).

This is in part a deliberate tactic of the Trump administration and its MAGA acolytes, something we addressed in the prior edition of this publication ("Flood the zone"). There we described the strategy, primarily promoted by ex-Trump political strategist Steve Bannon, to inundate voters and political opponents with news. The idea being that the Democrats will have a harder time to hit a moving target, and voters lose the 'signal' in the 'noise' and become indifferent to politics (something that works particularly well in the non-compulsory US voting system). This approach also has the parallel benefit of shifting what is known as the 'Overton Window'.

The Overton Window is a political concept that describes the range of ideas and policies that are considered acceptable to the mainstream population at a given time. For example, in the early days of Donald Trump's 2015 campaign, he made inflammatory comments about Mexican immigrants and also proposed a ban on all Muslims entering the United States. These comments and ideas were, at the time, considered shocking and unacceptable. However, whilst we do not contend that they are no longer shocking, we contend that a shift in the Overton Window has likely occurred and on a relative basis to many of the things that have since followed, it is no longer as shocking as it was at that moment 10 years ago.

When we contemplate the many and varied 'shocks' that have occurred in the year so far, we find that they tend to fall into one (or more) of three 'buckets'; Geopolitical, political and economic.

Geopolitical

This was the most anticipated of the three, given the return of Trump to the White House and his penchant for tariffs however, as has been widely acknowledged 'Trump 2.0' is not the same beast as his first presidential incarnation, and the surprise of his Liberation Day announcement is just one of the many challenges he's posed investors.

A broad list of geopolitical considerations includes:

- Trump/US
  - Aggressive and high tariffs
    - Both Japan and India had agreed deals, only to have them significantly change at the 11th hour.
    - The UK, in spite of its 'special' relationship suffered a 'good' deal of 'only' 10% tariff rate.
    - Attacks on traditional allies (particularly in the West) and embrace of traditional foes most notably Trump's affections for the likes of Vladimir Putin.
    - Summit in Alaska with Putin, despite no progress on Ukraine (the kind of thing that would traditionally enable a public meeting with a US president).
    - Alienation of India, in spite of a long-term strategic alliance, designed to counter China.
  - Generally, more aggressive military posturing
    - Renaming the "Department of Defence", the "Department of War".
    - Missile attacks on Yemen and alleged Venezuelan drug boats.
    - Bombing of Iran's nuclear facilities.
  - Transactional diplomacy
    - Qatar's $400m gift of a new presidential plane.
    - Trump's clear preference for political and business leaders to 'bend the knee' in the Oval Office, preferably baring gaudy gifts such as Apple CEO Tim Cook's 24 carat 'trophy'.
- China
  - Enjoying the appearance of being the 'adult' in the room, and positioning itself as a more reliable partner on the international stage
    - Has pushed back strongly on Trump and appears determined not to give the appearance of being bullied.
    - Recently hosted a military parade, to show its strength and potential preparation for the capture of Taiwan, sporting authoritarian guests including North Korea's Kim Jong Un, Russia's President Putin, India's Narendra Modi (not to mention Victoria's very own past Premier, Daniel Andrews).
- Russia
  - Despite continuing to be bogged down in Ukraine, has felt so emboldened as to start probing Europe's (i.e. NATO's) defences.
  - Appears to be conducting hybrid warfare, combining mis-information, hacking, and vandalism (i.e. arson on civil infrastructure) within Europe.
  - Shows no sign of changing course.

Political

In spite of a general environment of economic strength, large segments of discontent within the populations of many countries continues to drive combative politics.

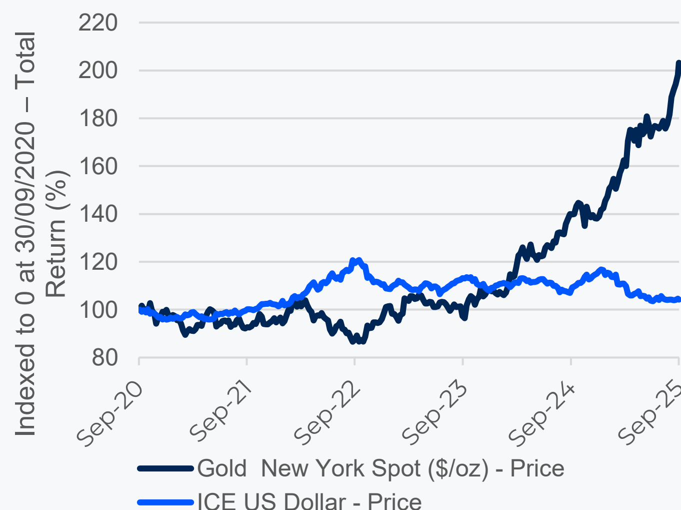
- France continues to lurch from one political crisis to another. Whilst this is not unusual in French politics, that President Emmanuel Macron is now on his 7th Prime Minister, is.
- Germany has seen an unwelcome swing back towards extreme-right wing politics, with the AfD (Alterative for Deutschland) party becoming the country's second largest political party.
- The UK has seen a collapse of the Conservative party, with Nigel Farage (he of Brexit fame) and his new Reform party, following Trump's MAGA flavour of populism and promising mass deportations, taking large swaths of traditional Tory support.
- It is not only countries that have had to contend with President Trump's rough-housing. Long standing democratic (as opposed to Democratic) institutions have been routinely attacked. The US military is being used for domestic policing (likely a breach of the Posse Comitatus Act). Additionally, the US government has started taking direct ownership in American companies, something that under a Democratic President would have been seen as 'socialist'. Not to mention the stark rise in political violence, which includes two assassination attempts on Trump himself, the attack on Nancy Pelosi and her husband (Nancy wasn't home at the time), the murder of both Minnesota state Democratic caucus leader Melissa Hortman and her husband, the shooting of Minnesota state senator, John Hoffman and his wife, and the public assassination of conservative podcaster and political firebrand, Charlie Kirk.

Economic

The economic backdrop has continued to face its own challenges, some emanating from the political and geopolitical spheres, some holdovers from the pandemic, and some more new developments. They include:

- Tariffs
  - Problematic from a diplomatic point of view but also threaten global trade and therefore economies. Indeed, the IMF now sees global growth running at 3.0% in the coming years, as opposed to the meaningfully higher 3.7% that was expected only 12 months ago.
- Employment
  - US employment continues to show signs of weakness, with the ratio of jobs-to-jobseekers now below 1x for the first time since the pandemic. Additionally, historic data has seen meaningful revisions lower. This is particularly acute in the under-25 age group, who are seeing unemployment levels greater than 10%.
- Inflation
  - Broadly continues to be higher than what was expected 12-months ago, restricting the ability of Central Banks to reduce interest rates, with threats that it may return.
- Chinese economic challenges highest in its modern history
  - Over-supplied property market continues to weigh heavily on the economy.
  - Demographic headwinds continue to threaten, with a drastic increase in births required to help maintain the labour force.
- Industrial revolution
  - The importance of AI is unlikely to be overstated – although its increasingly looking like people are trying. Just as with the original, steam-powered industrial revolution, the emergence of generative AI is likely to transform vast swaths of the business landscape. Whilst the benefits and implementation of the technology are still in their infancy, the implications for economies are enormous, with the potential to dramatically increase productivity on the positive side, but also to create unemployment as well as enabling greater fraud and dis-information. With the proverbial Pandora's box, now open, there is scope for a wide range of outcomes both positive and negative.
- Currency
  - The US dollar (USD) has lost some of the 'high gloss' shine given the reduced reliability of the US administration. Whilst USD remains the primary reserve currency in the world, central banks and investors alike are seeking greater diversification away from the US dollar than they otherwise might. Once described as an 'exorbitant privilege', the US may not be able to enjoy the capital financing advantage to the extent it once did.
  - The weakness of the US dollar has added to the strength of gold. Not a usual habitat of serious investors, gold is presently enjoying the status of a consensus trade. Although its implicitly negative cash flows make it difficult to confidently value, its ascension points to underlying vulnerabilities and concerns regarding long established economic architecture. As a result, it now exceeds 20% of global reserves at central banks.

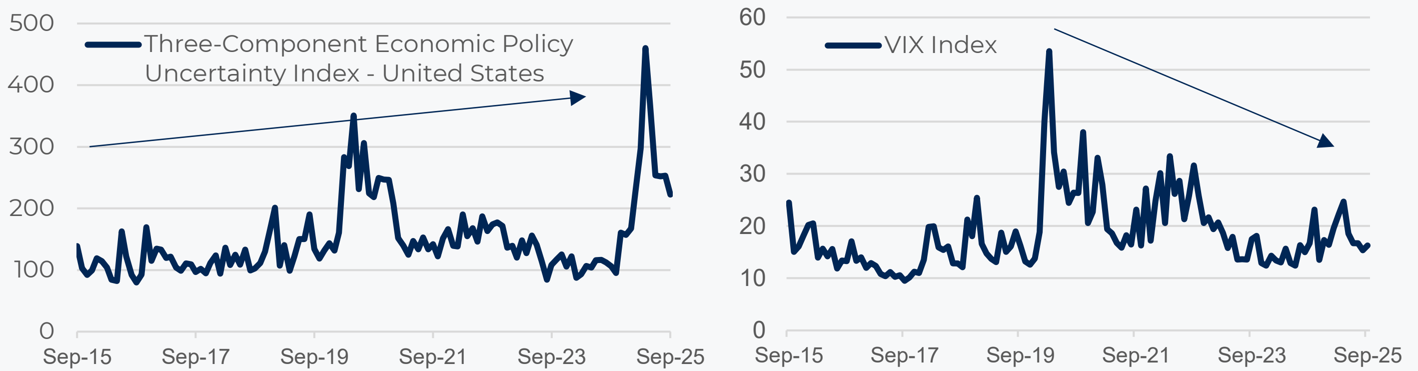
Chart 4: Gold vs USD chart



Source: Perpetual Private

- Uncertainty
  - A factor in of itself, the present level of disruption in trade, politics and civil discord, erodes the underpinnings of market foundations and threatens a market correction at some point in the future.

Chart 5: Uncertainty vs VIX – Does the market really hate uncertainty?



Source: FactSet, Perpetual Private

There is a well-known maxim that *markets hate uncertainty* / despite its elevated levels, they have not broken their stride. In the face of it (uncertainty) being at historically elevated levels, the VIX, a well-known indicator of fear in the market, continues to push towards lows (Chart 5).

This is not just unusual in the context. It is unusual through history. A compelling illustration of this fact is that August and September tend to be the softest months for equity market performance, whereas 2025 saw the best August for Australian shares in over a decade, and the best September for US shares in over 15 years (Chart 6).

Chart 6: September Effect charts – US vs Australia

	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec
10 Year Avg	0.8	0.1	0.6	1.3	0.9	1.1	3.4	0.1	-2.0	1.3	4.1	-0.1
US												
2025	2.7	-1.4	-5.8	-0.8	6.2	5.0	2.2	1.9	3.5	0.4		
2024	1.6	5.2	3.1	-4.2	4.8	3.5	1.1	2.3	2.0	-1.0	5.7	-2.5
2023	6.2	-2.6	3.5	1.5	0.2	6.5	3.1	-1.8	-4.9	-2.2	8.9	4.4
2022	-5.3	-3.1	3.6	-8.8	0.0	-8.4	9.1	-4.2	-9.3	8.0	5.4	-5.9
2021	-1.1	2.6	4.2	5.2	0.5	2.2	2.3	2.9	-4.8	6.9	-0.8	4.4
2020	-0.2	-8.4	-12.5	12.7	4.5	1.8	5.5	7.0	-3.9	-2.8	10.8	3.7
2019	7.9	3.0	1.8	3.9	-6.6	6.9	1.3	-1.8	1.7	2.0	3.4	2.9
2018	5.6	-3.9	-2.7	0.3	2.2	0.5	3.6	3.0	0.4	-6.9	1.8	-9.2
2017	1.8	3.7	0.0	0.9	1.2	0.5	1.9	0.1	1.9	2.2	2.8	1.0
2016	-5.1	-0.4	6.6	0.3	1.5	0.1	3.6	-0.1	-0.1	-1.9	3.4	1.8
2015	-3.1	5.5	-1.7	0.9	1.0	-2.1	2.0	-6.3	-2.6	8.3	0.1	-1.8

	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec
10 Year Avg	0.7	0.1	-1.0	2.0	0.1	-0.4	3.0	-1.0	-2.0	0.2	2.5	1.0
Australia												
2025	4.5	-4.2	-4.0	3.6	3.8	1.3	2.4	2.7	-1.3	1.3		
2024	1.1	0.4	2.6	-2.9	0.4	0.8	4.1	0.0	2.3	-1.3	3.3	-3.2
2023	6.3	-3.0	-1.2	1.8	-3.0	1.6	2.9	-1.4	-3.6	-3.8	4.6	7.1
2022	-6.5	1.1	6.4	-0.8	-3.2	-9.1	5.9	0.6	-7.4	5.9	6.1	-3.5
2021	0.3	1.0	1.6	3.7	1.9	2.1	1.1	2.0	-2.7	0.1	-0.9	2.5
2020	4.9	-8.3	-21.4	9.0	4.5	2.3	0.6	2.5	-4.0	1.9	10.0	1.2
2019	3.9	5.2	0.2	2.4	1.2	3.4	3.0	-3.0	1.3	-0.4	2.7	-2.2
2018	-0.4	-0.4	-4.2	3.7	0.6	3.0	1.3	0.6	-1.7	-6.2	-2.8	-0.5
2017	-0.8	1.6	2.6	1.0	-3.3	0.0	0.0	0.0	-0.5	4.0	1.1	1.6
2016	-5.5	-2.4	4.2	3.3	2.5	-2.7	6.4	-2.3	0.1	-2.2	2.1	4.1
2015	3.2	6.1	-0.6	-1.7	-0.2	-5.5	4.3	-8.5	-3.5	4.4	-1.4	2.5

Additionally, credit spreads continue to push towards historic lows, with providers of debt financing, requiring ever lower margins of safety. Whilst in normal times this would suggest highly confident investors, it is hard to square this with the simple reality that there is a lack of recent historical precedent for the current conditions, which therefore makes it impossible to adequately estimate levels of risk and return.

All of which suggest characteristics akin to that of a late cycle bull market, where investors remain invested primarily due to FOMO (fear of missing out). In this sentiment, we are reminded of the infamous testimony of then CEO of Citi Bank, after it faced collapse due to poor risk discipline in the run up to the Global Financial Crisis. When asked why the bank hadn't been more prudent, his response was simply "when the music is playing, you've gotta get up and dance". This isn't to say we are predicting an imminent crash in markets. Indeed, just as there are fragilities and weaknesses accruing on one side of the economic ledger, there are also meaningful strengths appearing on the other.

A little from column A, a little from column B

All of this considered, we see the coming months (and potentially years) as having heightened risks but also heightened rewards. There will likely be uncomfortable periods of being in-the-market but with a real risk of regret, should you miss out on what could be an impressively robust upside.

In order to properly monitor the risks of investing through such an environment, we find it helpful to consider a list of vulnerabilities alongside a list of opportunities, monitoring both as data emerges. Remembering that it is not only, what happens that matters, but the order in which it happens.

The prominent components on these lists include:

Opportunities

Artificial intelligence Has the potential to transform entire economies, if not societies, particularly with regards to productivity. Should it deliver on its promise, we could reasonably see one of the largest economic booms of all time, dramatically improving the length and quality of human lives across the planet.

Deregulation If Trump's slashing of government agencies enables an increase in entrepreneurial dynamisms, its benefits would likely be copied by other capitalistic countries, driving a self-fulfilling cycle of economic growth.

Strong consumer After the experience of staff shortages during the pandemic, companies have proven reticent to reduce workforces unless absolutely necessary. This has sustained low levels of unemployment, which has in-turn enabled resilient consumer spending – even after excess savings generated during the pandemic had been depleted. As long as this continues, so too should economic growth, particularly in the US. Helping this scenario further, is the presence of the 'wealth effect' whereby increases in asset values encourage consumer sentiment, which drives demand higher, which in-turn drives asset values higher again. Traditionally this has been most closely related to house prices, a clear benefit here in Australia (The Economist found in a recent study that a $1 increase in the value of an Australian home, drives an increase in spending by between 2 and 6 cents). In the US this is less prominent, as house prices have somewhat stagnated in the face of continued higher borrowing rates however, with retail investors participating in the US stock market more than ever before, it is arguable that increases in wealth via share portfolios may be similarly benefiting the confidence of the US consumer.

Momentum Markets have been shown over time to exhibit momentum as an underlying quantitative factor. Whilst there is much uncertainty in the current environment, what is not uncertain is that markets have been trending upwards for an extended period of time. Just as in physics, momentum in financial markets tends to persist until it either runs out of energy or is met by an opposing force. With the current enthusiasm, particularly for AI, it seems unlikely that the current environment will peter out. So, it therefore becomes more of a concern, to scan for anything that might be able to oppose the current trend – of particular concern would be a slowdown in capital investment into data centres, indicating a falling confidence in its potential to deliver shareholder value.

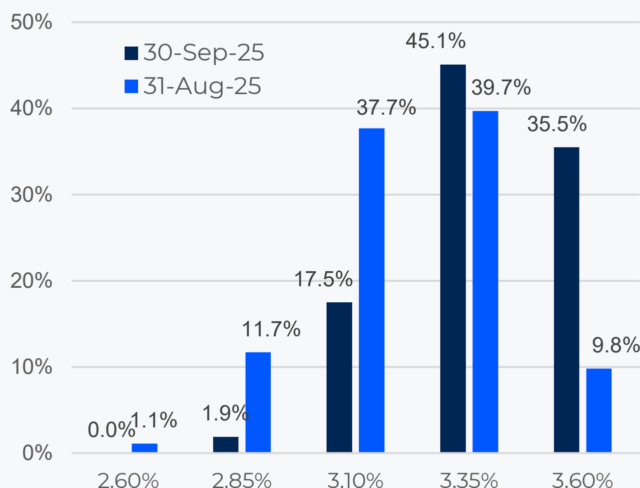
Vulnerabilities

Trade In spite of tensions around trade with the US largely retreating since April, there is nothing to suggest that the current balance is a 'stable equilibrium'. One thing Donald Trump hasn't proven to be, is predicable. He has shown to change his mind on a whim and we think it wise to expect that to continue. We see this as something that could potentially challenge markets in the coming months, particularly if he ever follows through on his more extreme threats. China has already begun to show itself to be more resistant to this challenge, using rare earths and soybean purchases, to exert pressure on the US, via the technology and farming sectors.

Artificial Intelligence Whilst AI has plenty of opportunity for upside, if its ascendancy stalls, or even slows, the economic ripples caused, may become tremors in parts of the global economy. In spite of trillions of dollars of investment, it is not yet profitable and so, much is rested on its success. Additionally, market sentiment has benefited so strongly from AI's emergence since early 2023, it is reasonable to assume that should that optimism dissipate, it has the potential for an outsized impact on markets.

Inflation With much hope pinned on a falling interest rate environment, inflation remains an important risk. Since its emergence during the pandemic, it has remained stubbornly persistent; a fact that we anticipated and has been reflected in our 'higher for longer' view of inflation and therefore interest rates. Whilst CPI is much closer to targeted ranges across much of the developed world, inflation has not gone away. Indeed, the Reserve Bank of Australia's September Monetary Policy Decision statement, loudly proclaims that "the decline inflation has slowed". So important was this to the RBA's communication that it is the name of the first heading within the document. Tight labour markets, trade disruption, AI power demand, property prices, are all threats to the inflation outlook and so require close monitoring.

Chart 7: Target Rate Probabilities – RBA Meeting (February)



Source: FactSet, Perpetual Private. Calculations are based on end of day closing prices from the FactSet Futures Prices Database.

Valuations As has been widely discussed, here and in the financial media, valuations across markets are relatively high. Though this can be justified by some of the fundamental data, it does place an explicit expectation on companies to maintain current and expected future levels of growth. This is achievable, however, the higher the valuation, the higher the expectation. Should the market be disappointed or lose confidence, selling pressure from investors adjusting to this new reality, could see asset prices compress.

Opportunity in a time of change

We began this report with a quote from Kristalina Georgieva, of the IMF. It therefore seems fitting to conclude by borrowing the title of her speech, "Opportunity in a time of change". That we are in a time of change seems to us to be undeniable. As investors, we see change as inherently opportunity laden. So, whilst we are cautious about the months and years ahead, we are not scared. Indeed, with the market consensus continuing to see a 'melt up' in asset prices, we see little reason to fight against such a trend.

As we have noted above, it makes little sense to resist a market that has built so much momentum however, one should not forget that these environments tend to be inherently unstable. As such our expectations from investment markets generally, are of higher risk but higher reward, with high growth, alongside elevated inflation likely to be core features.

Much has been said, in comparing today's technology boom to that of the 'dot com' bubble of the late 90s. Most importantly, this time around, revenue and earnings growth support the optimistic outlook whereas back then, "eyeballs" (literally the number of times a website had been viewed) were deemed an acceptable proxy of future earnings; they were not.

Equally, or perhaps more importantly, is that if we are indeed in the late stages of a tech-inspired market rally, we are also likely to see some explosive returns from here. The final months of the internet boom in the 90s, also saw the best returns. Whilst this rapidly receded once the bubble finally began to pop in the early months of 2000, it provided significant gains in wealth to those who were able to navigate it effectively.

As always, our view remains that diversification and caution are the best salve for investment positioning in exuberant markets. Maintaining a disciplined approach to risk, even amongst the potential excitement to come, will help avoid falling victim to any negative outcomes that may result when the cycle eventually turns.

Australian equities

Australian shares delivered solid gains over the September quarter. The S&P/ASX 300 rose 5.0%[1], extending the market's recovery from April's "Liberation Day" lows. Over the 12 months to 30 September, the index returned 10.8%. Smaller companies were the standouts, with the ASX Small Ordinaries climbing 15.3%[2] for the quarter and 21.5% year-on-year, supported by strong flows into emerging resource names and a boost from lower interest rates.

Macro conditions provided a mixed backdrop. The Reserve Bank of Australia cut rates by 25 basis points (bps) in August, taking the cash rate to 3.60%. However, inflation picked up with monthly headline CPI rising to 3.0%[32] year-on-year in August, its highest level in the past 12 months. Stronger-than-expected GDP growth in Q2, driven by the fastest household spending increase in three years, also tempered expectations for near-term easing. Employment data showed signs of softening, with weaker jobs growth leading unemployment to record a modest uptick. Still, Governor Bullock stressed in her September parliamentary statement that "while labour market conditions have eased a little...we assess that some tightness remains," underscoring the RBA's view that the jobs market is cooling only gradually.

At the sector level, performance was uneven. Materials (+21.2%[3]) were the clear standout, buoyed by a sharp rally in gold miners and renewed strength across base metals. Consumer Discretionary (+9.6%[4]) posted robust gains, aided by resilient household spending and a strong earnings season for retailers. Utilities (+11.4%[5]) also delivered double-digit gains, with the sector's performance largely driven by strong results and corporate developments at Origin Energy.

By contrast, Energy (-1.0%[6]) underperformed, dragged lower by the collapse of a takeover bid for Santos, which weighed on the broader sector. Health Care (-9.7%[7]) was another notable laggard, pressured by weakness in CSL and broader sector headwinds after the Trump administration announced 100% tariffs on imported pharmaceutical products. Consumer Staples (-1.4%[8]) also fell, with the decline led by Woolworths after its softer-than-expected results.

Financials ex-REITs managed a modest 1.3%[9] gain, with most of the major banks contributing positively. Commonwealth Bank was the notable exception, underperforming on valuation grounds after a strong run earlier in the year. Technology shares also delivered a muted return (+2.2%[10]), with gains constrained by weakness in sector heavyweights WiseTech and Xero, which offset broader strength in the smaller end of the sector.

From a style perspective, Value outperformed Growth in the quarter (+8.8%[11] vs -3.9%[12]), largely reflecting the outsized strength in commodity and resource-linked names.

Refer to footnotes' description on page 29

Chart 8: Australian shares – Large companies

Source: FactSet, Perpetual Private

Australian equities – Manager Insights and outlook

Heading into the September quarter, we were cautious on the outlook for Australian shares. Valuations across many areas of the market were already elevated, and while the prospect of lower interest rates provided a supportive backdrop, expectations for policy easing had run ahead of reality. By July, markets were pricing in two additional RBA cuts by year-end, which left little margin for disappointment. Against this backdrop, we anticipated heightened volatility during reporting season and positioned the portfolio with a style-neutral stance, while maintaining a modest underweight to the larger-cap segment of the market, particularly the banks, where valuations appeared stretched.

As expected, the August reporting season was highly volatile. Earnings downgrades outpaced upgrades by roughly three to one, and the market proved hypersensitive to results that fell short. Companies that missed expectations often experienced a sharp decline in value, while those that beat expectations were rewarded only modestly. Intra-day swings were more than double the long-term average, with nearly half of companies moving by more than 5% on their results day. Despite this, the broader market pushed higher, with the S&P/ASX 300 briefly flirting with the 9,000 level for the first time.

At the same time, several factors supported investor sentiment. The RBA delivered its third rate cut of the year in August, while indicators such as consumer and business confidence, retail sales, and house prices showed improvement. These dynamics helped sustain risk appetite and drove strong rotation into smaller companies, which outperformed large caps by more than 10% over the quarter and by a similar margin over the year. A key driver within small caps was the sharp rally in gold miners and with gold prices trading at all-time highs, which now account for around 15% of the Small Ordinaries index

From a style perspective, there was also a marked shift. Value stocks significantly outperformed Growth, as more richly priced companies came under greater pressure to deliver against elevated expectations. This rotation aligns with our preference to look further down the market-cap spectrum, where companies often present more compelling opportunities at more reasonable valuations.

Looking ahead, we remain somewhat cautious. Equity markets continue to trade near record highs and at premiums relative to history. A steady flow of capital from a variety of investors, including institutional superannuation funds, offshore investors attracted by Australia's relative stability, and retail allocations into ASX-listed ETFs, has provided an important source of support for equities, even as earnings growth has been underwhelming. While these flows and improving sentiment remain supportive in the near term, we believe a correction back towards more sustainable valuation levels is a distinct possibility, particularly if macro conditions soften or inflation proves sticky.

Against this backdrop, we are cautious about taking risk where we can't be comfortable of sufficient return potential, with us continuing to look primarily towards select opportunities among mid- and small-cap companies. These are the segments we expect to be the prime beneficiaries of lower interest rates and where we continue to find more attractive risk-reward opportunities.

International equities

International shares enjoyed another buoyant period, brushing off the complicated economic and geopolitical landscape, to return a robust 6.4%[13] for the quarter, and 2.3% for September; a month that is typically the weakest in the year. With the turmoil of President Trump's April 2nd tariffs announcement firmly in the rearview, markets have embraced a 'glass half full' perspective, opting instead to focus on the clear potential of the Artificial Intelligence (AI) revolution, over the haze of trade tensions and geopolitical conflict.

As such, the backdrop of global investment markets riding the continued and rapidly paced growth of AI and its related industries, has driven the performance of Growth companies over their Value peers, delivering 7.4%[14] over the 3 months to the end of September (vs 4.7%[15]) and 28.1% over 12 months (vs 17.2%). Indeed, when we look through a sectoral lens, Information Technology and Communication Services, both of which contain the main tech giants you would associate with the AI ecosystem, are the stand-out best performing sectors over the 3-month period returning 11.5%[16] and 10.5%[17] respectively.

Pleasingly however, markets more broadly have been basking in the positive market sentiment AI has inspired, along with the continued delays to Trump's tariffs and a robust consumer. Indeed, the third best performing sector (behind Information Technology and Communication Services) was Consumer Discretionary, which returned a respectable 8.4%[18] over three months. Even smaller companies have been enjoying farer conditions, returning 6.9% over the period, a healthy 0.7% higher than their larger company peers. This isn't to say that all segments of markets were strong. Consumer Staples was the only sector with a negative return for the quarter, receding -2.9%[19], taking its 12-month performance to 4.4% (in stark contrast to Communication Services' 40.8% for the same period). Real Estate and Health Care were also somewhat subdued (returning 1.5% and 2.1% respectively), as post COVID inflation and higher-for-longer interest rates weigh on their earnings and valuation multiple.

On a regional basis, Hong Kong's Hang Seng index was the best performing of the primary markets we follow, returning 12.2%[20]; a gain that outpaces that of the US' tech-heavy Nasdaq market at 10.2%[21] (also in local currency terms). A combination of Chinese government buying through state-owned enterprises, attractive valuation differentials and some positive developments in China's own tech industry, has been stoking share market returns across Asia. Trailing the pack, we saw Germany's DAX index consolidate with a -1.1%[22] return for the quarter, after some strong performance over the year (23.6%).

Refer to footnotes' description on page 29

Chart 9: International shares (local currency terms)

Source: FactSet, Perpetual Private

International equities – Manager insights and outlook

Following the April tariff announcement, investors adopted a more cautious stance given heightened apprehensions about trade policy and its economic implications. Nonetheless, this decline in confidence was transitory, with sentiment stabilising by May and risk appetite subsequently recovering. Equity markets have since advanced, reaching new highs, and reflecting a broadly constructive sentiment despite ongoing uncertainties.

US equities remain priced above historical averages, though a closer examination reveals subtleties. The S&P 500's valuation is notably influenced by a concentration of highly valued constituents; it would be inaccurate to characterise the entire US market as uniformly expensive. In fact, smaller-cap stocks generally present somewhat attractive valuations.

Within Emerging Markets, equities trade at a discount relative to developed markets, implying that growth risks and tariff concerns have largely been absorbed into current prices. Chinese corporates have demonstrated improving fundamentals against a challenging macroeconomic backdrop, with Emerging Market equities historically outperforming during periods of US dollar weakness.

Although valuations are a key consideration, earnings growth is the principal driver of equity performance. Corporate profit results have generally exceeded expectations in recent periods. While some organisations have withdrawn earnings guidance due to persistent macroeconomic uncertainties, management commentary has thus far indicated that tariff-related impacts have been limited. Analyst projections have, to date, been overly pessimistic regarding the effects of tariffs on margins, as firms have managed to mitigate costs either through price adjustments or operational efficiencies.

Within the United States, investment in Artificial Intelligence has emerged as a principal driver of economic momentum. According to JP Morgan, since the debut of ChatGPT in November 2022, companies engaged in AI have contributed approximately 80% of the S&P 500's earnings growth and 90% of capital expenditure growth. The remainder of the market is anticipated to deliver earnings growth of around 4% in the fourth quarter, illustrating a bifurcated economic landscape. It is important to keep in mind that semi-conductors are a cyclical sector, and demand can change quickly on the back of management decisions, particularly around the efficacy of AI integration into business practices and processes.

An emergent theme during the quarter has been a pronounced shift toward more cost-conscious consumer behaviour. With tariffs contributing to higher prices, consumers are demonstrating increased prudence and a heightened emphasis on value and affordability. The impact on consumer-oriented companies will vary according to each company's value proposition and its capacity to absorb or circumvent increased input costs. Businesses providing essential products, with robust supply chains, or those commanding strong brand loyalty are likely to prove more resilient, whereas companies more exposed to tariffs or facing weakening demand may experience greater pressure on margins and earnings growth.

It is our assessment that the margin for error has narrowed; earnings disappointments may be met with significant share price declines. Selectively avoiding higher-risk exposures will be critical to achieving strong investment outcomes. Moreover, we anticipate that the market will reward management teams exhibiting a sophisticated understanding of their supply chains and an ability to adapt to tariffs while safeguarding margins. Looking ahead, we expect a higher level of volatility throughout the final quarter of 2025, driven by uncertainties related to US trade policy, Federal Reserve decisions, and geopolitical developments. Nevertheless, such volatility may present compelling opportunities for discerning investors.

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Real estate

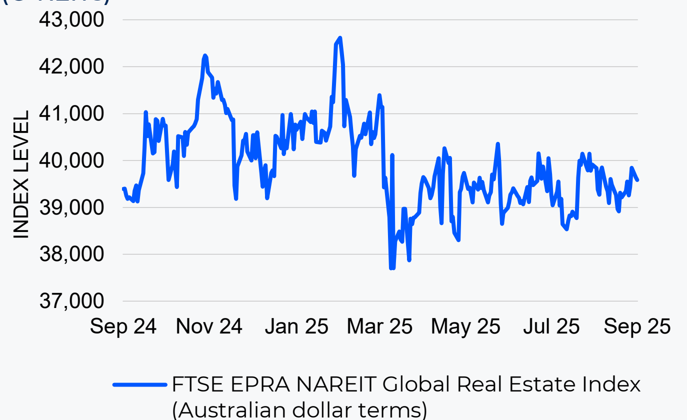
Listed Real Estate (as represented by A-REITs and G-REITs) broadly enjoyed relatively healthy returns over the third quarter of the calendar year. Domestically, Real Estate Investment Trusts (A-REITS) continued to recover from a challenging first half of 2025, breaking back into positive returns, year-to-date (YTD), before fading 2.9%[23] into the end of September. This resulted in a return of 4.8% for the 3-month period; mildly higher than the YTD tally of 4.3%. With inflation and therefore interest rates continuing to be 'higher for longer', diminishing expectations for rate cuts into the end of the year, weighed on valuations.

Across the Global REIT universe, the experience was similar to that here in Australia, with a general theme of recovery over the year (4.5%[24] YTD), a reasonable quarter (3.0%), with some softness in September (-0.3%). This isn't to say that every area within the asset class enjoyed such fair conditions. When we consider the outcomes across geographical regions, we notice a stark contrast in returns. Of the main regions we monitor, Germany was the notable laggard, falling 9.9%[26] in the three months, almost half of which was in September alone. In contrast, Japan saw some of the best conditions it has seen in years, gaining 9.9%[25] over the quarter and even posting a small positive return in September.

Chart 10: Australian Real Estate Investment Trusts (A-REITs)

Source: FactSet, Perpetual Private

Chart 11: Global Real Estate Investment Trusts (G-REITs)



Source: FactSet, Perpetual Private

Refer to footnotes' description on page 29

Real estate – Manager insights and outlook

REITs have underperformed broader equity markets, particularly offshore, but absolute returns remain positive. This is consistent with what we see as a constructive environment for existing landlords. We believe REITs are now trading near fair value, with limited exposure to the mega-cap technology companies that have been driving global equity markets higher—though there is some secondary exposure via data centres.

We've long highlighted the divergent outcomes between industrial and office property, but these sectors now appear to be converging: office is beginning to stabilise from its trough, while industrial is softening from peak conditions. Residential (globally) has been the more perplexing area of weakness. Higher interest rates and region-specific dynamics play a role, but given the housing shortages across Australia, the US, Canada, the UK, and Europe, fundamentals should support the sector over time. In the US, CBRE has reported rising absorption rates and falling construction pipelines, yet rental growth has been modest and volatile. A reversal in net migration trends may be a factor here and is a theme we will continue to monitor.

The third quarter produced mixed results locally. Healthcare stocks rebounded, Residential weakened further, with office and industrial delivering modest returns. Retail has been resilient, supported by firm consumer demand and a healthy transaction environment. While employment remains solid for now, any weakening in the labour market could weigh on retailers. In industrial, rental growth is being offset by higher incentives, leading to negative effective rental growth, while vacancy rates—though still low—are trending upwards. The sector also faces tariff-related risks, particularly in Australia where Goodman Group accounts for around 40% of the index. Regionally, weakness in Europe and the UK this quarter has tempered what was otherwise strong performance earlier in the year.

In the US, cash rate increases between early 2022 and mid-2023 disrupted the sector, but two years on, markets are adjusting. Over that period, returns have exceeded 10% p.a. globally and 20% p.a. domestically. REITs remain more sensitive to rate moves than broader equities, which explains some of the relative underperformance. Looking ahead, the core fundamentals for real estate remain supportive, but the key risk lies in a slowdown in economic activity that leads to job losses or weaker consumption. While not our base case, recent signs of softer US labour market data suggest this is a risk worth watching closely.

Alternatives

Growth alternatives

While there was optimism entering 2025 around an increase in merger and acquisition (M&A) activity, the first half of the year was mixed. Pleasingly, the September quarter has shown some green shoots, with exit activity starting to accelerate even as fundraising remains challenging for many general partners (GPs). Deal values stayed elevated, as sponsors pressed ahead with large-scale transactions such as the US$55 billion take-private of Electronic Arts. After a period of "watch and see," sponsors are beginning to launch sale processes on the back of improved sentiment. While there is still some way to go, overall deal volumes could reach 2024 levels by year-end.

Last quarter we noted the growing role of continuation vehicles (CVs) in providing liquidity to investors. Given the ongoing fundraising challenges, and the need for GPs to return capital to limited partners (LPs) to support future fundraising, this trend is continuing. We have begun due diligence on CVs and increasingly view them as akin to co-investment structures, offering better alignment between GPs and LPs as well as the potential to invest at modest discounts to holding value.

From a regional standpoint, Europe continues to offer relative value compared to North America. Entry prices are more attractive and the potential for fiscal stimulus could further support demand. German industrials, under pressure from high energy costs, are divesting non-core assets, creating carve-out opportunities for private equity (PE). To capture this, we upsized one of our European leveraged buyout (LBO) commitments. Despite the fluid backdrop, we remain disciplined in our PE approach, with a focus on valuation, financing structures, and manager operational capabilities. The fundraising environment remains stretched, with many GPs seeing longer fundraising cycles as LPs concentrate capital with top-tier managers.

Real estate markets also showed some turbulence. While transaction volumes remain weak, they were modestly higher than a year ago. We believe cap rate expansion has now peaked, creating more stable conditions. Against this backdrop, we continue to selectively pursue secondary LP interests in real estate funds where we can underwrite the underlying assets and their valuations. Discounts on secondaries are narrowing, however. More broadly, with central banks globally moving into easing cycles, we see potential support for the sector over coming periods.

Infrastructure saw an uptick in demand during the quarter after a lull in recent periods. Encouragingly, pricing remains sensible. Infrastructure remains a core holding across portfolios, valued for its stable and inflation-linked cash flows. Post quarter-end, one of our managers sold two assets at attractive premiums to holding value. While settlement will take time, both transactions are expected to be accretive to performance.

Across traded markets, dispersion in equity and credit pricing continues to reflect divergent macroeconomic and political conditions. Our existing credit exposures have delivered solid performance, but tighter spreads have reduced the appeal of new opportunities. In response, we are reallocating towards hedge fund strategies with asymmetric return profiles and relative value approaches, which offer resilience in risk-off markets. We are currently reviewing several opportunities and expect to make new allocations across late 2025 and into 2026.

Although sentiment around corporate activity is improving, we remain cautious on the pace of realisations, particularly in private equity where exits are likely to remain modest. We continue to pursue high total return, high cash flow investments while being selective in our allocations to private equity (both leveraged buyouts and growth equity) to ensure we manage our vintage year exposures.

Income alternatives

Demand for private credit assets remained robust through the September quarter, contributing to continued spread compression across multiple segments of private markets. Fixed-rate investments benefited from the decline in policy rates, while high-yield returns were positive but volatile. Broadly Syndicated Loans (BSLs) exhibited similar dynamics, currently delivering margins of approximately 1–2% above cash. The record issuance of Collateralised Loan Obligations (CLOs) in 2024 continues to underpin strong demand for BSL paper across the broader market.

Deal flow in private corporate credit remained subdued in Q3 2025, mirroring the slowdown in private equity where merger and acquisition (M&A) activity has been limited. Nevertheless, steady allocations to private credit strategies have ensured that new capital remains available for corporate refinancing and recapitalisation activity. While formal default rates remain low, we have observed a modest rise in out-of-court restructurings. When included, overall credit stress appears to have ticked higher. Encouragingly, the quick pace and orderly resolution of these restructurings suggest an efficient market response to emerging pressures.

Activity in the insurance-linked space has started to recover, though transaction volumes remain modest. Block trades continue to attract strong competition, keeping pricing for block liabilities elevated. As competition intensifies, we are seeing a gradual shift towards organic growth strategies. Within catastrophe risk, we anticipate a modest allocation to catastrophe bonds. While spreads have tightened slightly over the year, they remain attractive relative to other income-generating opportunities.

We continue to assess opportunities in specialty finance and regulatory capital markets. Specialty finance exposures remain among the strongest contributors to performance, and we are reviewing additional opportunities across both the US and Europe. Given the tightness in traditional corporate credit spreads, we expect to reallocate capital incrementally toward these sectors. Our ongoing review of the regulatory capital segment highlights wide dispersion in underlying asset quality and structural complexity. However, current market pricing across asset types does not yet appear to fully capture these differences in risk.

Income returns across the portfolio remain appealing, though further spread compression could moderate return potential over time. We remain constructive on the outlook for income alternatives but increasingly selective, focusing on credit-adjacent sectors that continue to offer healthy spreads and attractive risk-adjusted returns. With competition for yield elevated, opportunities are most compelling in niche or structurally complex areas such as specialty finance and regulatory capital. The portfolio maintains a defensive bias, balancing income generation with prudent liquidity management to remain flexible and responsive to potential credit dislocations.

Fixed income

Fixed income markets delivered modest returns in the quarter, as central banks continued to cut rates against a backdrop of higher inflation and still resilient growth. Global fixed income rose 1.0%[27], while Australian fixed income gained 0.4%[28]. Sovereign bond gains were constrained by sticky inflation, while credit outperformed with the support of tighter spreads, low default rates and healthy corporate fundamentals.

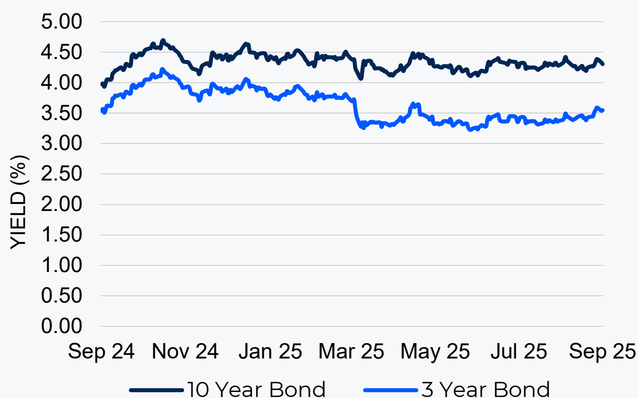
In Australia, the RBA cut the cash rate by 25 bps in August to 3.60%, its third reduction this year after earlier moves in February and May. Yields initially fell on the decision but reversed as August headline CPI surprised higher at 3.0%[32] year-on-year and GDP growth in Q2 beat expectations. Over the quarter, three-year bond yields climbed 29 bps to 3.55%, while the 10-year yield rose 14 bps to 4.30%. This left the Australian curve flatter, narrowing the difference between long- and short-term interest rates, underscoring how inflation continues to limit Australian sovereign bond gains despite easier policy.

In the US, the Federal Reserve cut rates twice in response to softer labour market data. US fixed income performance was supported by a decline in Treasury yields, with the most pronounced moves at the front end of the curve. Three-month cash rates fell nearly 40 bps, while two-year Treasury yields still edged higher by 10 bps to 3.61%. By contrast, the 10-year yield eased just 8 bps to 4.15%, leaving the 2s–10s curve flatter. The long end of the curve remained relatively anchored, held up by fiscal risks, inflation expectations, and concerns about threats to Fed independence. Across Europe, moves were more modest, with German 10-year bund yields up 12 bps and French 10-year yields up 26 bps, reflecting renewed investor concerns over long-term debt sustainability.

Credit markets continued to perform strongly as spreads compressed further. Australian credit returned 0.9%[29], while global investment grade spreads tightened to multi-decade lows, supported by solid corporate fundamentals and low default expectations. Investment grade credit returned 2.0%[30] over the period. Global high yield also performed well (+2.5%[31]), buoyed by resilient corporate earnings and strong demand for carry. With prevailing spread levels now trading at historical tights, valuations leave little room for disappointment if growth slows or defaults begin to rise.

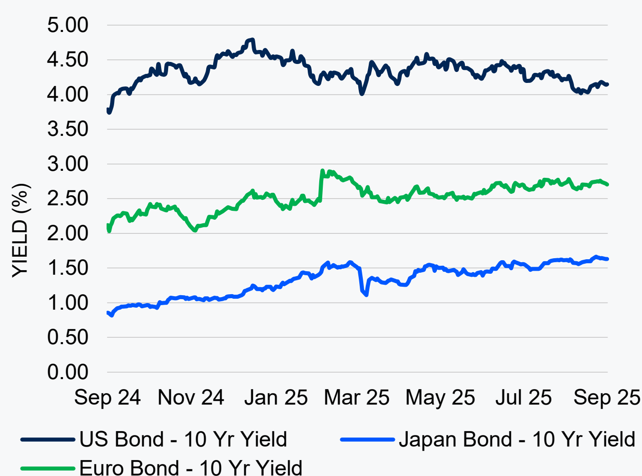
Refer to footnotes' description on page 29

Chart 12: Australian government bond yields



Source: FactSet, Perpetual Private
Note: Bond prices are inversely correlated with bond yields.

Chart 13: Global government bond yields



Source: FactSet, Perpetual Private

Chart 14: Global credit markets

Source: FactSet, Perpetual Private

Fixed income – Manager insights and outlook

Following the August rate cut, the RBA has shifted to a more cautious, data-dependent stance. While inflation has edged higher, it remains within the Bank's 2–3% target band. Volatility in government bond markets has persisted, driven largely by offshore developments. To date, there has been no sustained increase in Australian inflation attributable to US trade policy. However, our base case is for US inflation to rise over time. Discussions around tariff pass-through suggest that corporates have not yet fully passed on all tariff-related costs, though many anticipate doing so over the coming year.

The long-term implications of US trade policy remain uncertain. In the near term, we expect upward pressure on US inflation and a weaker medium-term growth outlook, though resilient consumer spending continues to provide support. This policy uncertainty and its inflationary consequences have been a key driver of ongoing volatility in global sovereign bond markets. An environment we expect to persist.

Despite falling policy rates, absolute yield levels remain elevated relative to historical norms, particularly when compared to the pre-2022 zero-rate environment. Credit demand has remained strong, with spread compression supported by subdued M&A activity and a weak issuance pipeline. While spreads are tight, we believe there is scope for further tightening, particularly in a declining policy rate environment. Lower base rates are also supportive of credit quality, improving overall debt serviceability.

Within portfolios, we have been constructive on select parts of the government bond curve and have taken advantage of opportunities in Emerging Market (EM) debt, which has been a key contributor to returns in recent periods. This has been complemented by credit selection focused on the one- to three-year segment of the curve. However, at this stage of the cycle, we believe much of the alpha in EM and government bonds has already been realised, and we expect to gradually reduce our overweight positions in both areas over the coming months. We continue to maintain a selective approach within credit, emphasising shorter-dated exposures where valuations remain more attractive.

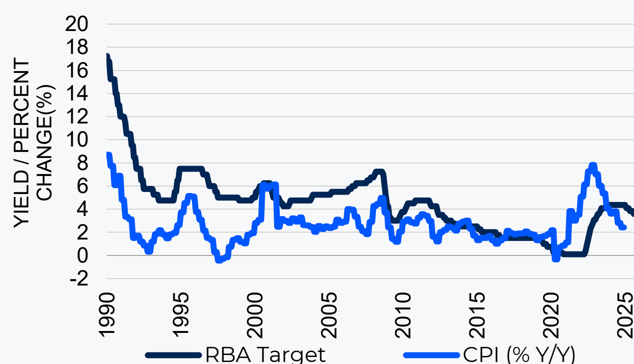
Australian cash rate

The Reserve Bank of Australia (RBA) lowered the official cash rate by 25 basis points to 3.60% at its August meeting, marking the third cut since the easing cycle began in February. So far, the Bank has delivered one reduction each quarter, broadly consistent with the pace it had outlined earlier in the year.

The decision came against a backdrop of mixed data. Inflation has moderated overall but surprised to the upside more recently in August, with monthly CPI lifting to 3.0%[32] year-over-year – within the RBA's 2–3% target band – but highlighting persistent price pressures in certain categories. Labour market conditions also showed signs of loosening, with total employment falling modestly and participation edging lower to 66.8%. However, the unemployment rate held steady at 4.2%, still low by historical standards, and the RBA has noted that the labour market remains "a little tight."

The RBA has signalled a cautious and data-dependent stance, noting that policy remains well placed to respond to incoming inflation and employment data, as well as to developments in the global economy.

Chart 15: Long-term cash rate vs inflation



Source: FactSet, Perpetual Private.

Australian cash rate – Outlook

Looking ahead, the RBA appears to be nearing the end of its current easing cycle. While another 25bp cut cannot be ruled out by early 2026, the upside surprise in inflation and resilience of the labour market mean the case for continued easing is weakening. Wage growth, in particular, is being closely monitored. If labour market conditions remain tighter than expected and wage pressures persist, the Board may decide that policy has already moved far enough and pause sooner than markets anticipate.

Governor Bullock has repeatedly emphasised that future moves will be driven by the data. Underlying inflation continues to drift toward target, but services inflation and housing costs remain sticky. This dynamic leaves the RBA in a wait-and-see posture, weighing the risk of cutting too far against the need to support growth.

Overall, while another cut remains possible, the balance of risks now points to the RBA being close to done with its quarterly cadence of easing. A more durable assessment will depend on upcoming inflation and labour market releases, which will determine whether policy has already reached an appropriate level or whether further adjustments are required.

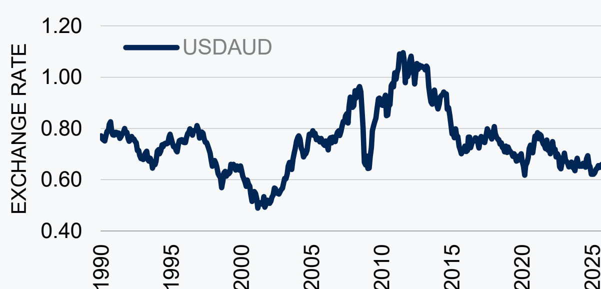
Refer to footnotes' description on page 29

Australian dollar

The Australian dollar (AUD) marginally appreciated over the September quarter, gaining 1.1% against the US Dollar (USD) to close near US$0.66. Volatility persisted, albeit at a lower magnitude than in the first half of 2025, with the AUD/USD trading range fluctuating between US$0.64 and US$0.67. The AUD saw a steady decline in July and August as strong US economic data showed that higher tariff rates had yet to meaningfully dent US growth, before recovering into quarter-end.

The quarter saw several factors impacting the AUD but not one decisively moving the currency in either direction. Domestically, the Reserve Bank of Australia (RBA) August rate cut initially weighed on the currency, but the upside surprise in monthly August CPI (3.0% year-on-year) tempered expectations for further easing. In the US, signs of labour market weakness prompted the US Federal Reserve (Fed) to cut rates twice during the quarter, placing downward pressure on the USD. The US Dollar Index – a measure of the greenback's value against a basket of major currencies – finished the quarter broadly flat. This marked a pause after a material weakening through the first half of the year, leaving the USD consolidating at current levels and contributing to the AUD's narrow trading range.

Chart 16: Australian dollar US dollar (daily) long term



Source: FactSet, Perpetual Private.

Australian dollar – Outlook

The Australian dollar enters the final quarter of 2025 under a cloud of caution, having remained range-bound for much of the September quarter. It will likely take a catalyst such as diverging Chinese data, a shift in tone from the Fed, or a more hawkish RBA to push the currency out of its trading band.

The RBA is expected to deliver at most one further 25 basis point cut by early 2026, though the upside surprise in August CPI (+3.0% year-on-year) suggests the easing cycle may be nearing its end. By contrast, the Fed faces a more difficult balance. Inflation has crept higher (2.3% year-on-year in April to 2.9% in August), while labour market data has softened. Having already cut rates twice in the September quarter, the Fed is expected to lower rates further before year-end.

Valuation models continue to suggest the AUD is undervalued, with purchasing power parity estimates suggesting it should be closer to US$0.72. However, the currency remains subdued, with volatility relatively low and only fresh economic data likely to alter the near-term narrative.

One additional factor for the outlook is the role of institutional investors, particularly superannuation funds. Market participants are watching closely for any increase in currency hedging on US equities and other offshore assets. A September speech by RBA Deputy Governor Andrew Hauser noted that nominal hedge levels will inevitably rise over time as super fund inflows grow but stopped short of signalling a material shift in hedge ratios. For now, arguments against materially higher hedging remain compelling: the AUD remains positively correlated to global equities, hedging carries a cost, and FX volatility is low. These dynamics have limited the incentive for funds to lift hedge ratios in the near term.

[1] As measured by the S&P/ASX 300 – Total Return index

[2] As measured by the S&P/ASX Small Ordinaries – Total Return index

[3] As measured by the S&P/ASX 300 Materials (Sector) – Total Return index

[4] As measured by the S&P/ASX 300 Consumer Discretionary (Sector) – Total Return index

[5] As measured by the S&P/ASX 300 Utilities (Sector) – Total Return index

[6] As measured by the S&P/ASX 300 Energy (Sector) – Total Return index

[7] As measured by the S&P/ASX 300 Health Care (Sector) – Total Return index

[8] As measured by the S&P/ASX 300 Consumer Staples (Sector) – Total Return index

[9] As measured by the S&P/ASX 300 Financials ex-REITs (Sector) – Total Return index

[10] As measured by the S&P/ASX 300 Information Technology (Sector) – Total Return index

[11] As measured by the MSCI Australia Value – Net Return index

[12] As measured by the MSCI Australia Growth – Net Return index

[13] As measured by the MSCI All Country World index in AUD terms

[14] As measured by the MSCI World Growth index in AUD terms

[15] As measured by the MSCI World Value index in AUD terms

[16] As measured by the MSCI AC World - Information Technology index in AUD terms

[17] As measured by the MSCI AC World - Communication Services index in AUD terms

[18] As measured by the MSCI AC World – Consumer Discretionary index in AUD terms

[19] As measured by the MSCI AC World - Consumer Staples index in AUD terms

[20] As measured by the Hang Seng Index in AUD terms

[21] As measured by the NASDAQ Composite in AUD terms

[22] As measured by the German DAX in local currency terms

[23] As measured by the S&P/ASX 300 A-REIT index

[24] As measured by the FTSE EPRA Nareit Global index in AUD terms

[25] As measured by the FTSE EPRA Nareit Japan index in AUD terms

[26] As measured by the FTSE EPRA Nareit Germany index in AUD terms

[27] As measured by the Bloomberg Global Aggregate (AUD hedged) index

[28] As measured by the AusBond Composite (0+Y) index

[29] As measured by Bloomberg AusBond Credit (0+Y) index

[30] As measured by the ICE BofA Global Corporate (AUD Hedged) index

[31] As measured by the Bloomberg Global High Yield (AUD Hedged) index

[32] Australian Bureau of Statistics (ABS), National Accounts, and Consumer Price index

[33] EconoTimes, “AI Capex to Surge in 2025 as Hyperscalers Boost Spending, Says BofA”. Available at: “AI Capex to Surge in 2025 as Hyperscalers Boost Spending, Says BofA - EconoTimes”.

[34] Morgan Stanley, “Who will fund AI’s $3 trillion ask?”. Available at: https://www.morganstanley.com/insights/podcasts/thoughts-on-the-market/ai-investing-credit-markets-andrew-sheets#:~:text=And%20however%20large%20AI%20is,centers%20and%20their%20hardware%20alone.

[35] Artificial Intelligence Market Report 2025, Available at: https://www.startus-insights.com/innovators-guide/artificial-intelligence-market-report/.

[36] Association for the Advancement of Artificial Intelligence (AAAI), 2025 survey of 475 respondents, cited in Financial Times, July 2025.

[37] As measured by S&P 500 index in AUD terms

[38] As measured by the France CAC 40 index in AUD terms

[39] As measured by the MSCI AC World Small Cap index in AUD terms

[40] As measured by the MSCI AC World - Real Estate index in AUD terms

[41] As measured by the MSCI AC World - Health Care index in AUD terms

Authors

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Andrew provides investment research, portfolio construction and bespoke investment advice for Perpetual Private's clients.

Andrew works closely with advisers by providing specialist investment knowledge on Perpetual's investment process and strategy implementation, focusing on delivering optimal solutions to our stakeholders and partners. This is further augmented by his provision of transparent and accessible knowledge of financial markets and asset classes both globally and locally.

Having spent 15 years in London, Andrew returned to Melbourne with a wealth of international experience to benefit Perpetual's clients and partners. Having started his career working on private equity transactions and stock market listings, he then spent time working on equity trading desks, before moving into investment management. In his role as a Portfolio Manager for Barclays Investment Solutions, Andrew managed money across multiple asset-classes on behalf of various client groups, before focusing on the charity and not-for-profit segment. With responsibility for as much as £3bn in assets, he developed a strong reputation for delivering robust investment performance linked to his comprehensive understanding of global investment markets.

Andrew is a holder of the Chartered Financial Analyst and the Chartered Alternative Investment Analyst designations.

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Hugo is an Investment Specialist at Perpetual Private, where he joined the Investment Research Team in October 2023. He supports the Head of Managed Accounts and Perpetual Private Investment Directors by developing and maintaining investment content and collateral. He also helps communicate Perpetual Private's investment offerings to advisors and intermediary sales teams, representing the Multi-Manager and Direct Equities teams.

Before joining Perpetual, Hugo gained valuable international experience working as a Research Analyst for a wealth management firm in Vancouver, Canada. During his four years there, he focused on strategic and tactical asset allocation for high-net-worth clients across diverse asset classes and client profiles. Prior to his time in Canada, he held roles in Sydney at BT Financial Group as a Customer Relations Consultant and TP ICAP as a Trainee Broker.

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